FOR PROFESSIONAL INVESTORS ONLY

Q2 2018

Quarterly Newsletter

Sanlam FOUR Global Equity Fund

Performance Review

In Q2 2018 the fund was roughly flat in USD terms, underperforming the broader equity index which rose 1.7%. The majority of the positive performance came from our Energy, Discretionary and Healthcare positions.

Key Facts	
Fund AuM	£144.7m
Strategy AuM	£180.4m
Number of Holdings	57
Active Share	89.5%
Yield	2.8%
Tracking Error	3.0%
VaR	4.9%
% in cash	2.0%

	Inception	QTR	YTD	1Yr	3Yrs	5Yrs	Since Inception
A Accumulation GBP	27/04/11	6.5	0.6	4.1	8.9	8.3	7.7
MSCI World		8.1	2.9	9.3	15.0	13.0	11.7
B Accumulation USD	09/09/11	0.5	-1.4	6.7	3.5	6.0	9.0
MSCI World		1.7	0.4	11.1	8.5	9.9	11.1

Performance beyond one year is annualised.

12 Months to	Jun-18	Jun-17	Jun-16	Jun-15	Jun-14
A Accumulation GBP	4.1	27.6	-2.7	3.8	11.0
MSCI World	9.3	21.6	14.4	10.3	10.0
B Accumulation USD	6.7	23.6	-15.9	-3.6	25.1
MSCI World	11.1	18.2	-2.8	1.4	24.0

Source: Sanlam FOUR, Morningstar and Lipper as at 30/06/2018.

Past performance is not an indicator of future performance.

Market Recap

Equities recovered ground during Q2 rallying 1.7% in aggregate but coming off higher levels on several occasions as macro-political worries escalated. Macro data shows the US is enjoying the lowest level of unemployment since April 2000. With inflation nudging higher, the Fed raised rates by 25bps but tightened its outlook with two further increases now expected for the year. European macro data has been weaker, justifying the ECB's dovish stance on maintaining negative rates and declaring an end to new QE stimulus by year end. The People's Bank of China (PBOC) lowered bank reserve ratios freeing up liquidity as US dollar strength and trade concerns hit the Renminbi.

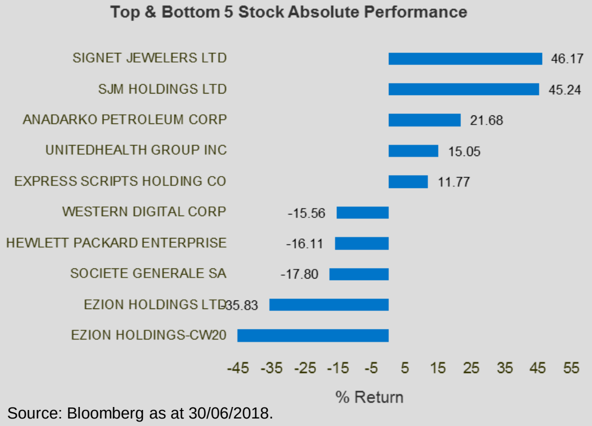
President Trump's campaign threat to impose heavy tariffs on Chinese goods moved a step closer with the imposition of tariffs on $34bn of goods out of a program of US$50bn, with suggestions of two further rounds of US$200bn to come. China responded with tariffs focusing on agriculture and autos. Europe responded on steel and aluminium tariffs with an increase in duty on EUR2.8bn on US goods.

The nervousness and negative sentiment had a relatively greater impact on exporting countries with Japan, China, Germany and South Korea all falling. Sectors and sub-sectors with complicated supply chains such as Industrials, Semiconductors and Autos also underperformed.

Political turmoil rocked Europe with Italy seeing an unlikely coalition between the anti-establishment left and populist right. Early fears of an anti-Euro position have been replaced by fears of an unfunded increase in government spending commitments. Spain also saw political turmoil with long standing PM Mariano Rajoy falling to a no confidence vote and replaced with an unlikely broad coalition of remaining parties. Elsewhere, Mexico saw the election of 'former' left-wing firebrand Andres Manuel Lopez Obrador and Brazil was volatile with a trucker's strike polarising the political debate ahead of elections in October.

Oil continued to rally as supply shortages in Venezuela and sanction induced shortages in Iran firmed up the market. Combined with a strong dollar, the impact on energy importing emerging markets was a clear negative. The disparity between 'growth' and 'value' indices continues with growth once again providing all the appreciation in markets with value remaining flat.

Performance Attribution



Source: Bloomberg as at 30/06/2018.

Companies like Anadarko (+21.7%), SJM (+45.2%), Signet Jewelers (+46.2%) and Express Scripts (+11.8%) were the primary contributors this quarter. UnitedHealth (+15.1%), ENI (+8.3%) an Imperial Brands (+10.6%) also performed admirably.

Anadarko and ENI were lifted up by the tightening oil market which pushed the barrel price all the way to $79 by quarter end. Signet Jewelers rebounded sharply after posting a much better than expected quarter, demonstrating healthy underlying growth metrics across its brands. We ultimately believe the business can leave behind its mostly self-inflicted problems and growth organically ahead of the industry while generating good returns on capital. The last set of results gives credibility to our thesis.

Express Scripts resumed its positive trajectory as the regulator cleared the AT&T/ Time Warner merger, paving the way for a successful Cigna/Express Scripts takeover.

Conversely the fund was held back by our European Financials like Societe Generale (-17.8%), Intesa Sanpaolo (-14.2%) and BNP Paribas (-11.4%) as well as DRAM suppliers Samsung Electronics (-11.1%) and Western Digital (-15.6%). Tupperware Brands and HP Enterprise also detracted from overall performance.

European Financials fell on the result of the Italian elections and the protracted inability of the leading parties to form a credible government; while the weakening digital memory pricing hit both Western digital and Samsung.

In the quarter we initiated a position in Reckitt Benckiser, Dow-Dupont and Merck, while selling out lift boat operator Ezion Holdings. Reckitt is a long term compounder that receded significantly over the past two years, on reasons that we believe are short term in nature. Merck has a significantly undervalued immune-oncology franchise; while in Dow Dupont we are playing a long term restructuring story under a respected management team.

Market Outlook

After a strong surge over the last 18 months, the outlook for corporate profits is becoming more uncertain. We say this not from a belief in an economic crystal ball but simply that the list of market areas with visibly depressed profits is getting shorter (primarily European financials and Energy) whilst those with above average historic profitability is lengthening. At the macro level, US profit to GDP is already comfortably above average and appears to have already rolled over. Forecasts for economic growth remain positive (they always are!) but risks to profits from tight labour markets, rising commodity prices and interest rates are growing, not to mention the potential fall-out from a trade war.

Market valuations have contracted modestly in the face of these uncertainties, with aggregate valuations on world markets standing in line with their historic averages. These market averages conceal a wide divergence, however, as the market has sought ‘safety’ from increased economic worries by chasing the valuations of a handful of growth companies ever higher, whilst leaving the rest of the market to languish. This has left the spread of valuations in the market at wide level compared to history (not quite yet at the 1999 peaks). This is a two-edged sword to investors; on the one hand it provides the opportunity to build a portfolio of companies at attractive discounts to market indices but makes these market favourites increasingly vulnerable to disappointments.

Our investment process and disciplines have led us to respond to these conditions in two ways. Firstly, our focus on sustainability of earnings has rotated us away from some of the more cyclical parts of the market towards those with room to expand earnings or simply less cyclical earnings streams. The portfolio has neutralised the pro-cyclical earnings tilt it has shown for the last couple of years. Secondly, we have stuck to valuation disciplines, allowing us to create a portfolio which is valued at significant discounts in terms of what we are paying for assets, earnings, dividends or cashflows. Despite this discount, aggregate earnings growth expectations are similar to the wider market averages. We expect the combination to support superior returns and resilience over time.

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Important Information